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No. 86-1053

In the Supreme Court of the United States

OCTOBER TERM, 1986

COMMISSIONER OF INTERNAL REVENUE, PETITIONER

v.

ASPHALT PRODUCTS CO.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

REPLY MEMORANDUM FOR THE PETITIONER

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TABLE OF AUTHORITIES

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1. In our petition, we explained that the court of appeals' method of computing the negligence penalty cannot be squared with the explicit and unambiguous language of Section 6653(a) and that it runs counter to 68 years of consistent judicial construction and to the expressed intent of Congress. Indeed, the fact that the negligence penalty is computed as 5% of the entire underpayment of tax is so well established that it did not even occur to respondent to challenge that mode of computation in the Tax Court or in the court

of appeals. Rather, the Sixth Circuit's unprecedented reading of the statute was aired in its opinion *sua sponte* without the benefit of briefing or argument by either party. See Pet. 4-10.

Respondent's brief in opposition confirms that the court of appeals' holding is without foundation. Respondent makes no effort to suggest how that holding can possibly be reconciled with the terms of the statute. Indeed, apart from a caption to its argument (Br. in Opp. 2), respondent does not even contend that the court of appeals' decision is correct. In response to our assertion (Pet. 8) that the decision below is contrary to "every other decision that has considered this aspect of Section 6653(a)," respondent addresses only one of the cases that we cited. Compare Br. in Opp. 2-3 with Pet. 8-10. And in the one case that respondent does discuss—*Abrams* v. *United States*, 449 F.2d 662 (1971)—the Second Circuit squarely held, contrary to the Sixth Circuit below, that the negligence penalty must be computed as 5% of the *total* underpayment, not as 5% of the portion of the underpayment (in *Abrams*, about one sixth) that was attributable to the taxpayer's negligence. See Pet. 8-9. In the end, respondent seeks to explain the unprecedented nature of the holding below by asserting that this is a case "of first impression" (Br. in Opp. 2) in which the taxpayer's negligence was responsible for a relatively small portion of the deficiency. But as we explained in our petition, the courts have confronted this situation before and have uniformly held that the statute must be construed as Congress wrote it, notwithstanding taxpayer pleas about the supposed "harshness of the result." See *Bianchi* v. *Commissioner*, 66 T.C. 324, 335 (1976), aff'd, 553 F.2d 93 (2d Cir. 1977) (Table).

Because Congress intended the negligence penalty "to act as a deterrent" (*Abrams*, 449 F.2d at 664), the courts (apart from the court below) have correctly rejected such pleas and have given Section 6653 the meaning that its words unambiguously require.

2. Respondent's chief basis for opposing our petition for certiorari is its assertion that the Sixth Circuit's error has little prospective importance because its impact "has been * * * limited by Congress" (Br. in Opp. 5) to pre-1987 tax years. Respondent points, as did we (Pet. 7-8), to a statement in the Conference Report on the Tax Reform Act of 1986 that explicitly addresses the decision below and concludes that the decision "inaccurately states present law." 2 H.R. Conf. Rep. 99-841, 99th Cong., 2d Sess. 782 n.3 (1986); Pet. App. 89a. In respondent's view, this Report has "little bearing on the interpretation" of Section 6653 as it applies to pre-1987 tax years, but it "does evidence congressional intent as to how § 6653(a)(1) should be applied for tax years after 1986" (Br. in Opp. 4-5). Accordingly, respondent contends that this case does not warrant the Court's attention.

This contention is flawed in several respects. First, even if one assumes arguendo that the Sixth Circuit will not regard its decision in this case as binding for post-1986 tax years, allowing the decision to stand could frustrate congressional intent with respect to many taxpayers whose pre-1987 tax liabilities have not yet been determined. Many taxpayers have not yet even filed their 1986 tax returns, and many returns for previous years have not yet been audited. The Commissioner asserted more than $144 million in negligence penalties during 1985 alone (see 1985 Comm'r of Internal Revenue Ann. Rep. at 67),

and, given the frequency with which the statute of limitations is extended by mutual consent (I.R.C. § 6501(c)(4)), negligence penalties remain assessable for many prior years; this case, for example, involves respondent's tax liability for 1974. Moreover, the decision below will create considerable administrative problems for years to come. Tax Court cases appealable to the Sixth Circuit will likely be burdened by evidentiary proceedings directed at determining the existence of negligence for each individual item on the return—an inquiry that is unnecessary under a correct reading of Section 6653(a). See Pet. 13.[1]

Second, it is by no means clear that the Sixth Circuit will regard its decision in this case as having been superseded for post-1986 tax years. Although respondent professes certainty that the 1986 Conference Report will eliminate the prospective effect of the decision, that certitude is difficult to reconcile with respondent's assertion that the Report has "little bearing" on the interpretation of Section 6653(a) for years prior to 1987. The language of Section 6653(a) was in no way changed by the Tax Reform Act of 1986. Thus, if the construction of that section enunciated by the court below is allowed to stand, there is no assurance at all that the Sixth Circuit will hold the same language to have a different meaning from 1987 onwards.

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[1] The IRS estimates that there are 4,923 cases now pending in trial courts, primarily in the Tax Court, that are appealable to the Sixth Circuit. In the experience of the IRS, a negligence penalty under Section 6653(a) is asserted, on the average, in 20%-25% of all cases docketed in the Tax Court. In 1986, the negligence penalty was involved in more than 30% of the cases in which the Tax Court rendered opinions.

In our view, it is appropriate for the Court to act now to forestall the uncertainty and administrative problems that will be engendered by the untenable decision of the court of appeals. Such action need not impose any substantial burden on the Court. Given the absence of any suggestion by either the court of appeals or respondent as to how the decision below can possibly be reconciled with the language of the statute, this case presents a straightforward and discrete question of statutory interpretation that can be resolved without the necessity for plenary review. See, *e.g.*, *Rodriguez* v. *United States*, No. 86-5504 (Mar. 23, 1987). Alternatively, the Court may wish to remand the case to the court of appeals to enable it to consider the 1986 Conference Report, which was not before it when it rendered its decision. See Pet. 8 & n.4, 14.[2]

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[2] Respondent also contends (Br. in Opp. 3, 5-8) that this case is not an appropriate one in which to resolve the correct interpretation of Section 6653(a) because the courts below erred in finding that respondent was negligent at all. This contention is irrelevant to the merits of our petition. Respondent's claim of lack of negligence is an attack on the judgment below, not an alternative ground for affirmance that would be before the Court if the petition here were granted. The claim is properly raised by respondent, by way of supplemental brief, in its own petition (No. 86-1054). As we have explained in opposing that petition (86-1054 Br. in Opp. 10-11), we believe that respondent's challenge to the determination of negligence is insubstantial. But if the Court disagrees, we think that the proper course would be to grant review of both questions, rather than to leave intact the Sixth Circuit's erroneous and unprecedented holding as to the computation of the negligence penalty.

For the foregoing reasons and those stated in our petition, it is respectfully submitted that the petition for a writ of certiorari should be granted.

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APRIL 1987

☆ U. S. GOVERNMENT PRINTING OFFICE: 1987 181483 40293